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SUBJECT: SCENESETTER FOR PARIS III

Classified By: Jeffrey Feltman, Ambassador, per 1.4 (b) and (d).

IMPORTANCE OF PARIS III LARGER
THAN FINANCIAL, REFORM ISSUES

¶1. (S) On the surface (and this is what we recommend emphasizing in our public messages), the January 25 Paris III conference is about Lebanon's proposed reform program and the financial assistance Lebanon needs to get through 2007 and move toward more sustainable debt levels. Lebanese from across the political spectrum recognize that, financially, a successful Paris III is good for Lebanon -- all of Lebanon. The pro-Syria March 8-Aoun opposition to the pro-independence Siniora government has thus muted its criticism of the conference accordingly and tried to shift the focus to "labor" and other disputes. But, with Paris III taking place against the backdrop of a deepening governmental crisis sparked by the November resignation of six pro-Syria ministers, the political stakes are in fact as high as the financial stakes. While Paris III can contribute to Lebanon's financial stability, the survival of the Siniora cabinet and the ability of the March 14 majority to beat back Syrian and Iranian influence in Lebanon are also linked to Paris III. For the GOL, a successful Paris III will create financial breathing space, support a credible reform program, and strengthen PM Siniora and the March 14 majority -- goals that we share. For the March 8-Aoun opposition that wants to reverse the March 14 gains from 2005, the trick of Paris III is how to ensure Lebanon wins financial support to avoid an economic meltdown, while preventing the GOL from getting the political bounce we want the conference to provide.

ONGOING POLITICAL CRISIS
LINKED TO PRO-SYRIA AGENDA

¶2. (S) The fact that the French are hosting a conference envisioned to take place in Beirut over a year ago -- the original plan was Beirut I in November 2005, not Paris III in January 2007 -- demonstrates the severity of the political and security crises plaguing Lebanon. Lebanon is still struggling with the aftermath of 33-day Hizballah-Israeli war. And just since early November, Lebanon has experienced the resignation of six cabinet ministers (with the departure of all five Shia ministers putting the legitimacy of the Siniora cabinet in question), the assassination of a March 14 cabinet member, several large-scale demonstrations demanding a new cabinet, an ongoing sit-in that has effectively crippled Beirut's commercial core, a halt to progress in establishing the Special Tribunal for Lebanon, renewed arms smuggling from Syria, harsh rhetoric and localized clashes

against UNIFIL (that hint at possible attacks against UNIFIL), reports of increased al-Qaida presence, and dashed expectations regarding Arab mediation. Credible security concerns have forced ministers, MPs, and other political leaders to retreat into a kind of voluntary house arrest.

13. (S) These problems are all linked to the quest of pro-Syria Lebanese to derail the Special Tribunal, reverse UNSCR 1701's restrictions of Hizballah's freedom of movement in the south, divide and weaken the March 14 majority that came to power as Syrian influence receded in 2005, and ensure a pliant pro-Syria successor to President Emile Lahoud when the Parliament selects the new president by November. While there are tactical differences within the March 8-Aoun alliance -- Michel Aoun, for example, wants early parliamentary elections, an anathema to Nabih Berri -- there is unified insistence on acquiring by any means possible sufficient cabinet strength (more than a third of the seats) to block any cabinet decision and topple the government at will. Especially after analyzing Nasrallah's 1/19 television interview, we do not anticipate Hizballah backing down. Michel Aoun's harsh anti-GOL rhetoric over the weekend has also dampened the quiet, intermittent communication between Aoun and PM Siniora.

AFTER LACKLUSTER OPPOSITION RALLIES,
HIZBALLAH, AOUN PROMISE ESCALATION

14. (S) Heading into Paris III, we expect the environment in Lebanon to worsen this week. In his 1/19 television interview, Hizballah Secretary General Hassan Nasrallah raised the rhetorical stakes and spoke as someone looking for

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escalation, not compromise and solutions. To the annoyance of Saudi Ambassador Khoja who has been shuttling among the various players, Nasrallah's positions derailed Arab mediation. A day after Nasrallah's remarks, the March 8-Aoun opposition announced a general strike to begin on 1/23. Previous threats of escalation resulted in little action on the ground, of course, but this time Nasrallah seems to have decided to employ his personal prestige to reverse the impression of an opposition movement losing steam and to counter images of PM Siniora sitting in Paris with world leaders. Michel Aoun and pro-Syrian politicians like Suleiman Franjeh have engaged in fear-mongering over the weekend, in hopes that even those people who don't support the Tuesday strike will stay at home to avoid problems, thus making adherence to the strike appear larger.

15. (S) While it is risky to make predictions about surprise-filled Lebanon, it seems probable that a partially observed general strike will take place on Tuesday that will include attempts to close roads and burn tires. These actions are no doubt intended to shift the media story away from Paris III and reinforce the opposition's claim that the Siniora cabinet is illegitimate. By escalating in this way, Hizballah and its allies cannot be blamed for derailing Paris III but can wrest media attention away from Siniora's success in Paris and put a question mark over the whole Paris proceedings. If the opposition can provoke Lebanese security services to fire upon demonstrators, so much the better: pictures of Siniora smiling with world leaders will be gleefully juxtaposed by the pro-Syria press here against images of security services (especially the Sunni-commanded ISF) under Siniora's government's command beating up or killing Lebanese. At the same time, the longer the political crisis continues, the more legitimate the Shia grievances will be in at least one aspect: the lack of Shia ministers in Siniora's cabinet (created when the Shia voluntarily withdrew on 11/11) is indeed contrary to the cross-sectarian balance of power enshrined in Lebanon's political structures.

SINIORA, CABINET REMAIN STEADFAST;

¶6. (S) In the face of all of this, PM Siniora, his 17 remaining cabinet ministers, and March 14 leaders more generally have shown unexpected resilience and steadfastness. To the extent possible given the extraordinary security precautions they must take, the cabinet ministers have attempted to carry on business as normal, including by passing reforms such as the establishment of the Telecommunications Regulatory Agency (an essential step toward telecom privatization) long blocked by President Lahoud. Hassan Nasrallah, Michel Aoun, and other pro-Syria political figures are reported to be unpleasantly surprised that the Siniora cabinet did not collapse within a day or two of opposition rallies. Ironically, the Sunni-Shia tensions -- heightened by the Hizballah-dominated opposition rallies directed against the PM (an office considered a Sunni institution) -- have worked until now to moderate opposition behavior: the Shia seemed unwilling to cross lines (such as storming Siniora's office, an option that Michel Aoun apparently once favored) that would have provoked sustained Sunni-Shia clashes. One of the favorite topics of political speculation here is whether and when Hizballah will decide (or be ordered by Syria or Iran) to cross that line. We guess that Nasrallah now hopes for Sunni-Shia clashes, but in a way where the Sunnis are seen as the provocateurs and the Shia the victims. (Ergo, Nasrallah's largely successful attempt to discredit the ISF as a "Sunni militia"; any problems with the ISF will be seen as Sunnis beating up on Shia.)

PARIS III SHOULD STRENGTHEN SINIORA
AGAINST PRO-SYRIA OPPOSITION

¶7. (S) Paris III will not cure Lebanon of these security, sectarian, and political problems. Nor is Paris III a vehicle that will by itself promote the kind of sorely needed intra-Lebanese dialogue that (with the exception of the occasional channel between Aoun and Siniora) is entirely absent during this crisis. But a successful Paris III conference will reinforce the legitimacy of the Siniora cabinet by virtue of the world leaders in attendance. Having

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sat with high-level Arab and western officials, in a conference presided over by French President Chirac and including the Secretary and UNSYG Ban Ki-Moon among its participants, Siniora will have renewed strength and resolve to face the pro-Syria critics back home. Those in Lebanon who have been fence-sitting -- waiting to see which side of the March 8/Aoun-March 14 divide prevails -- will be more likely to stick with the Siniora cabinet and March 14 majority, in recognition that a cabinet headed by a pro-Syria figure like former PM Omar Karami would be unable to attract such international attention and needed financial support to Lebanon.

¶8. (S) Because of Paris III, should negotiations -- whether direct or via an Arab intermediary -- resume between the GOL and the opposition, Siniora will be in a relatively better bargaining position because of a successful Paris III. But, particularly in light of the anticipated general strike this week, we recommend scrubbing all public remarks for words and phrases that Nasrallah could use to claim that Paris III was a "Sunni" victory that does little for the already angry Shia. Rather than praise Fouad Siniora, in other words, we should find ways to reinforce the basic message that Paris III is good for all of Lebanon. In our view, the fact that success will inevitably accrue to Siniora from a successful Paris III should be a key byproduct, not the primary public aim. (In this regard, we think that talking publicly about "Lebanon" and the "Lebanese government" rather than the "Siniora government" will probably help Siniora deflect criticism at home.)

A SUCCESSFUL CONFERENCE CAN REMOVE
THE IMMEDIATE FINANCIAL THREATS

¶9. (S) Most importantly, a successful Paris III should help Siniora overcome one of the very real dangers to his government: a February financial crunch, when more than USD 1 billion comes due, in a combination of a maturing Eurobond issue and payment dates for letters of credit for fuel deliveries. (Lebanon's debt is somewhat front-loaded, with USD 16 billion coming due in 2007-08. Presumably most of this will be refinanced.) Without Paris III, the financial markets have shown little interest in further exposure here. At first, it seemed that Aoun and other opposition figures rubbed their hands in gleeful anticipation of a looming financial crisis that would further weaken the Siniora cabinet. Now, we have the impression that even the opposition leaders recognize the gravity of Lebanon's financial circumstances and will not go so far as to derail Paris III: no one wants to be blamed for preventing a successful outcome. Siniora, Finance Minister Jihad Azour, and Central Bank Governor Riad Salameh consider the cash and commitments promised at Paris III as both important in their own right and vital to stimulating private-sector capital flows to Lebanon. If Paris III can restore the financial markets' confidence in Lebanon, then Siniora, his cabinet, and March 14 leaders have one less crisis on which they must focus their efforts.

LONGER TERM GOALS: PROMOTING REFORM,
MOVING DEBT LEVELS TOWARD SUSTAINABILITY

¶10. (S) Besides giving an immediate, tangible political boost to the Siniora cabinet at a critical time -- which is the unstated goal -- Paris III also has the stated goal of supporting a serious reform program with the potential of putting Lebanon's debt-to-GDP ratio (now exceeding 185 percent) on a downward trend, toward eventual sustainability.

Inter alia, the proposed reform program -- deemed to be a serious effort by the IMF, World Bank, and other experts -- attempts to enhance revenue collection, reduce waste, establish a sensible social safety net, shrink the bureaucracy by attrition, eliminate patronage institutions, reduce subsidies in fuel prices, and build a platform for economic growth.

¶11. (S) Even though the progressive introduction of tax hikes will not begin until 2008 in recognition of the economic hardships caused by the Hizballah-Israeli war, Siniora and his economic advisors did not design a program for political expediency. We understand, in fact, that Siniora and his ministers had to work hard to convince their own political patrons such as Walid Jumblatt and Saad Hariri

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to sign on (which both eventually did), given measures that are bound to be unpopular and limit the ability of political bosses to use public funds for patronage. In a pleasant surprise after the GOL's abysmal public outreach efforts regarding post-war reconstruction, the GOL launched a major public relations blitz to explain the reform program through advertisements, seminars, ministerial appearances on talk shows, etc. Besides the widely available 29-page Paris III reform paper, the GOL has a large number of related sectoral studies provided to those working in specific areas. While no doubt there are plenty of things to clarify, criticize, or amend within the GOL's plans, most observers agree that the GOL (with plenty of assistance) has, this time, done its homework.

¶12. (S) The key will be implementation, which is why we hope Paris III will have both upfront contributions (to stimulate the private-sector capital flows and help the GOL pay its February bills) and staged, conditioned disbursements

that will serve as incentives for performance. After Paris II in November 2002, President Emile Lahoud and his cronies within the (then) Rafiq Hariri cabinet succeeded in derailing the promised reforms. Now, opposition figures like Aoun sniff that Siniora -- who was Finance Minister at the time of Paris II -- seeks a quick fix of cash but will repeat his history of non-implementation. While we do not want to publicly admonish Siniora (and give his critics material to use against him), our private messages to Siniora, in our view, should emphasize the need for steady implementation. In addition to the donor commitments linked to performance, the GOL is also interested in an IMF program (the Emergency Post Conflict Assistance program) -- this, too, is unlike Paris II and will help inject much-needed discipline into the process.

MANAGING EXPECTATIONS

¶13. (S) The March 8-Aoun opposition will try hard to downplay Paris III. Given how high the political and financial stakes are for the Siniora cabinet and pro-independence March 14 majority, managing expectations is an important and complicated task. In making the preposterous claim that Paris III will raise upwards of USD 12 billion in grants and concessional loans, the pro-Syria media in Lebanon has already done its part in raising unreasonable expectations -- in hopes that the more modest sums to be achieved at Paris III will lead to widespread disappointment among the average Lebanese. (Remembering the accusations that Siniora's friendship with us did little to protect Lebanon during the Hizballah-Israeli war, we can already envision the headlines and speeches by the pro-Syria opposition now: "Look, all of Siniora's international friends brought little to Paris. What good is Siniora, then?")

¶14. (S) At the same time, Siniora and his economic advisors themselves seem to have exaggerated notions of what Paris III will bring. Although they are careful not to give out numbers in public, they have told us privately that they hope for USD 6-9 billion overall and USD 1.5-2 billion in upfront cash. While we defer to those in Washington who have been tracking potential grants and concessional loans for more accurate analysis, this range strikes us as high. Siniora and his advisors need to leave Paris convinced of the conference's success, even if the actual amounts are lower than the sums in their flights of wishful thinking.

FELTMAN